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No. 99-

IN THE

Supreme Court of the United States

SUSAN A. DESIDERIO,

Petitioner,

v.

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

PETITION FOR A WRIT OF CERTIORARI

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QUESTIONS PRESENTED FOR REVIEW

1. May petitioner be forever barred from her chosen profession in the securities industry because she refuses to consent to mandatory arbitration of all future employment disputes, as a non-negotiable condition of employment in the industry, under an arbitration system that fails adequately to protect workers' statutory, common law, and constitutional rights?

2. Is the mandatory arbitration requirement in the securities industry system unenforceable under the Federal Arbitration Act, Title VII, or other state or federal employee protection statutes?

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Petitioner respectfully submits that a writ of certiorari should issue to review the judgment of the United States Court of Appeals for the Second Circuit in this case.

OPINIONS BELOW

The opinion of the Court of Appeals is reported at 191 F.3d 198 (2d Cir. 1999) and is reprinted in Appendix A hereto at 1a-22a. The District Court's opinion is reported at 2 F. Supp. 2d 516 (S.D.N.Y. 1998) and is reprinted in Appendix B at 23a-34a. The Judgment of the District Court is reprinted in Appendix C at 35a-36a. The Order of the Court of Appeals denying rehearing is reprinted in Appendix D at 37a-38a.

STATEMENT OF JURISDICTION

The Order of the Court of Appeals affirming the District Court's opinion of March 18, 1998 was dated and entered on September 22, 1999. The Order of the Court of Appeals denying petitioner's motion for rehearing was dated and entered on November 2, 1999. This petition is timely filed within 90 days of the Order of the Court of Appeals. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1). Petitioner first invoked federal court jurisdiction in the case under 28 U.S.C. §§ 1331, 1332 and 5 U.S.C. § 701, *et seq.*

STATUTES AND REGULATIONS INVOLVED

The following statutes are involved in this case: Title VII of the Civil Rights Act of 1964, as amended by the Civil Rights Act of 1991, Pub. Law 102-166; the Federal Arbitration Act, 9 U.S.C. § 1, *et seq.*; and SEC Regulation 17 C.F.R. § 240.15b7-1 (1993). The pertinent texts of these statutes and regulations are set forth in Appendix E at 39a-44a.

STATEMENT OF THE CASE

On March 18, 1996, petitioner Susan A. Desiderio was hired as a securities trader by Suntrust Bank of Florida ("Suntrust"). Pursuant to federal law and SEC regulations, all persons employed as securities traders in the United States are required to sign securities industry Form U-4, which registers the trader

with one or more national exchanges (in this case respondent National Association of Securities Dealers, Inc. ("NASD")). The Form U-4 registration requires the trader, as a condition of employment, to comply with and to be bound by all of the exchanges' SEC-approved rules including, in this case, the NASD's rule mandating arbitration of any employment-related dispute.[1]

Petitioner signed the Form U-4 on March 18, 1996, but struck out the mandatory arbitration provision because she was not willing to waive her right to proceed in court, before a jury of her peers, on future employment claims. Petitioner informed Suntrust that she would not agree to the mandatory arbitration requirement but would accept all the other conditions of the Form U-4. Suntrust did not object to Desiderio's modification of the form and stated its willingness to employ petitioner without requiring mandatory arbitration of later-arising employment disputes. However, respondent NASD refused to accept petitioner's attempted modification and informed Suntrust that an altered Form U-4 was unacceptable for its securities trader's federally-required registration.

Desiderio refused to execute the Form U-4 as long as it required mandatory arbitration of employment disputes. Because NASD refused to permit Desiderio to register without binding herself to mandatory arbitration, Suntrust was forced to terminate Desiderio's employment. Desiderio then brought this action, contending that the securities industry's mandatory arbitration requirement deprived her of her constitutional and statutory rights to a jury trial and to an Article III court on future claims. She further alleged that the NASD's mandatory arbitration procedures were legally inadequate to protect the substantive statutory rights of employees, like herself, who may have Title VII discrimination or other statutory employment

1. Although the SEC in June 1998 approved the NASD's proposed modification of this rule to exempt statutory employment discrimination claims arising after January 1, 1999, that change came far too late to benefit petitioner.

claims. Desiderio sought an opportunity to prove in court that the NASD arbitration scheme she would have been compelled to accept was, in fact, an inadequate substitute for a judicial forum. Petitioner now seeks certiorari both to resolve the circuit conflict concerning what constitutes an inadequate forum for mandatory non-judicial resolution of employment disputes and to resolve the conflict concerning whether the securities industry's SEC-approved arbitration rules constitute state action, thereby triggering "unconstitutional conditions" analysis.

I. Petitioner Desiderio's Complaint

In her January 15, 1997 complaint, Desiderio asserted that the Form U-4 mandatory arbitration provision violated her statutory rights under Title VII, 42 U.S.C. §§ 2000e to e-17, her constitutional rights under Article III and the Fifth Amendment Due Process Clause, and her right to a jury trial under the Seventh Amendment. Desiderio sought a declaratory judgment invalidating the mandatory arbitration provision in Form U-4, and also sought compensatory damages under her pendent state common law claims for NASD's tortious interference with her employment and its negligent infliction of emotional distress. The complaint named both the NASD and the SEC as defendants.

II. The District Court's Order

In a judgment entered on April 23, 1998, the United States District Court for the Southern District of New York (Leisure, J.) granted defendants' motions to dismiss Desiderio's complaint for failure to state a claim pursuant to Rules 12(b)(6) and 12(b)(1) of the Federal Rules of Civil Procedure. Petitioner appealed from that judgment. She later stipulated to a withdrawal of her appeal against the SEC, leaving the NASD as the only appellee.

III. The Court of Appeals' Decision

The Second Circuit affirmed, invoking *Gilmer v. Interstate/ Johnson Lane Corp.*, 500 U.S. 20 (1991) to hold: (1) with respect to Title VII claims, Congress did not intend "to preclude the

waiver of judicial remedies"; (2) "compulsory arbitration does not defeat the right to compensatory and punitive damages or fee shifting because an arbitrator is also empowered to grant this kind of relief"; (3) "arbitration may be compelled in this case, since only the forum — an arbitral rather than a judicial one — is affected . . ."; (4) "NASD is a private actor, not a state actor" and the SEC's mere approval of Form U-4 "is not sufficient to justify holding the state liable for the effects of the arbitration clause"; and (5) petitioner Desiderio has no private right of action against NASD. Rehearing was denied on November 2, 1999.

REASONS FOR GRANTING THE WRIT

A. Desiderio's Fact-Specific Challenge To The Adequacy of NASD's Mandatory Arbitration Procedures Alleged the Egregious Unfairness of Such Procedures

In *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20 (1991), this Court rejected a facial challenge to securities industry arbitration based on a worker's "speculative" and "generalized" assertion that the New York Stock Exchange's mandatory arbitration scheme was not adequate to protect statutory rights. The Court explicitly noted, however, that its ruling was not intended to preclude future fact-based challenges to the adequacy of mandatory arbitration in the securities industry, and indeed, the Court invited such challenges "for resolution in specific cases." 500 U.S. at 33. *See Cole v. Burns Int'l. Security Servs.*, 105 F.3d 1465, 1482 (D.C. Cir. 1997) ("Obviously *Gilmer* cannot be read as holding that an arbitration agreement is enforceable no matter what rights it waives or burdens it imposes."). This case presents precisely such a fact-based challenge to the adequacy of the NASD arbitration scheme as it operates in actual practice. *See* A-14[2] (Compl. ¶ 29) More broadly, it raises the important issue of what constitutes an "adequate" non-judicial forum for the resolution of fundamental anti-discrimination rights.

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2. "A-" refers to the specified page of the Joint Appendix below.

The allegations of Desiderio's complaint, which must be accepted as true in the procedural context of this case,[3] assert that mandatory securities industry arbitration is woefully inadequate to protect the common law, statutory, and constitutional rights of securities traders like petitioner Desiderio. More specifically, petitioner's complaint alleges:

> • The NASD Arbitration Manual expressly instructs NASD arbitrators that they are not required to follow statutory law in resolving employment disputes, and NASD arbitrators routinely fail to apply governing statutory law in Title VII and other employment discrimination cases. (Compl. ¶ 29g)
>
> • The NASD affirmatively discourages any awards of punitive damages by arbitrators, and requires any arbitration award that includes punitive damages secretly to be reviewed by the NASD staff before it is released to the parties. (Compl.¶ 29h)
>
> • NASD arbitrators commonly impose onerous and exorbitant "forum fees" on employee litigants, which accumulate at the rate of up to $3,000 per day, notwithstanding the cost-shifting provisions of Title VII and other employment-discrimination statutes. (Compl. ¶ 29j)
>
> • NASD arbitrators regularly refuse to award attorneys' fees to prevailing plaintiffs, even when those plaintiffs prevail on statutory grounds that would entitle them to a statutory fee award in civil litigation, thereby undermining the "private

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3. The district court dismissed petitioner's complaint pursuant to Rules 12(b)(1) and (6). The Court of Appeals reviewing the dismissal *de novo* stated that ". . . we accept all of plaintiff's factual allegations in the complaint as true and draw inferences from those allegations in the light most favorable to the plaintiff." 191 F.3d at 202.

attorney general" enforcement mechanism on which civil rights laws and other protective employment laws depend for their effectiveness.[4] (Compl. ¶ 29k)

• The NASD actively discourages its arbitrators from including written findings and conclusions in their awards or indeed from providing any meaningful explanation of their decisions, in order to render judicial review of those decisions difficult or impossible.[5] Accordingly, NASD arbitration awards rarely include written findings of fact or conclusions of law. (Compl. ¶ 29c)

• The demographic characteristics of NASD arbitrators are unrepresentative of the community of arbitrators qualified to decide employment disputes, but rather are drastically skewed in favor of older, white males who have formerly worked in management positions for the securities industry, principally because of the NASD's internal referral procedures for selecting arbitrators, which perpetuate this imbalance.[6] (Compl. ¶ 29d, e, f)

• Although NASD panel arbitrators theoretically have discretion to permit formal discovery, in fact such discovery is not customarily available or permitted and indeed the practice is discouraged during the training of arbitrators. (Compl. ¶ 29i)

Desiderio was confronted with a Hobson's choice when faced with the NASD's refusal to accept her modification of the Form U-4. Either she had to sign the Form U-4 and thereby

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4. *See DiRussa v. Dean Witter Reynolds, Inc.*, 121 F.3d 818 (2d Cir. 1997), *cert. denied*, 522 U.S. 1049 (1998).

5. *See* NASD arbitration training document entitled "If We Wanted Your Opinion We Would Have Asked For It". (A-135-147)

6. *See* GAO Report entitled "How Registered Representatives Fare in Discrimination Disputes". (A-103-134)

accept the NASD mandatory arbitration scheme with all its substantive and procedural inadequacies or, instead, she could stand on her principles and be forever barred from employment in her chosen profession for *any* United States securities company. Petitioner brought this action to obtain a judicial determination that she could not be relegated to such an inadequate forum and forced to give up her right to pursue future employment claims in court, and to obtain damages for her resulting injuries.

1. The NASD's Mandatory Arbitration Procedures Do Not Adequately Protect Employees' Substantive Statutory Rights

This Court and several circuit courts have made clear that a mandatory arbitration clause cannot be enforced if the arbitration procedure it requires does not provide an adequate, alternative forum for protecting statutorily-provided rights and benefits.[7] In *Gilmer*, the Court rested its decision upholding

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7. *See Gilmer, supra*, 500 U.S. at 28, *quoting Mitsubishi Motors Corp.*, 473 U.S. 614, 637 (1985) (binding arbitration of statutory rights may only be compelled "so long as the prospective litigant may effectively vindicate [his or her] statutory cause of action in the arbitral forum"); *Alexander v. Gardner-Denver Co.*, 414 U.S. 36, 51, 56-58 (1974) ("there can be no prospective waiver of an employee's rights under Title VII" where the purported waiver requires the employee to adjudicate his statutory claims before a tribunal of labor arbitrators who are required to apply the "law of the shop," but not the law of the statute); *Graham Oil v. ARCO Products*, 43 F.3d 1244, 1247 (9th Cir. 1994), *cert. denied*, 516 U.S. 907 (1995) (mandatory arbitration clause cannot be enforced against party lacking equal bargaining power if arbitration would deprive that party of "statutorily-mandated rights and benefits that Congress intended them to possess"); *see also Cole, supra*, 105 F.3d at 1468 ("we read *Gilmer* as requiring the enforcement of arbitration agreements that do not undermine the relevant statutory scheme"); *id.* at 1482 ("At a minimum, statutory rights include both a substantive protection and access to a neutral forum in which to enforce those protections"); *Paladino v. Avnet Computer Technologies, Inc.*,

(Cont'd)

securities industry arbitration on the assumption, not contradicted by the scant record before it, that arbitration under the NYSE rules merely traded one effective forum (*i.e.*, accessible and outcome-neutral) for another. Desiderio's complaint, however, alleged that the NASD securities arbitration forum did *not* adequately protect the statutory rights of Title VII and other employment discrimination claimants, but made the exercise of those rights unduly expensive and impermissibly subjected those rights to the unfettered discretion of inadequately-trained, non-neutral arbitrators who are told they are required neither to follow the law nor to explain the reasoning underlying their decisions.

Desiderio's complaint identifies at least three separate reasons why securities industry arbitration fails adequately to protect a worker's substantive rights.

a. Securities Industry Arbitrators Not Required to Follow the Law

First, Desiderio's complaint (¶ 29g) alleges that securities industry arbitrators are expressly instructed in *The Arbitrators Manual* that they are *not* required to follow "case precedent or statutory law" in deciding employment cases. Thus, securities industry arbitrators have no obligation to apply Congress' carefully-developed standards under Title VII or similar statutes, or to consider the extensive case law construing those often difficult-to-apply standards.

Title VII is an exceedingly complex statute. Its effective enforcement requires neutral decisionmakers trained in the law's nuances who are required to decide cases based upon the statutory language and applicable case precedent. That is why Congress vested ultimate authority for enforcing Title VII rights

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(Cont'd)

134 F.3d 1054, 1062 (11th Cir. 1998) (separate opinion of Cox, J., joined by Tjoflat, J.) ("When an arbitration clause has provisions that defeat the remedial purpose of the statute, . . . the arbitration clause is not enforceable").

in federal judges, who have expertise in construing statutory language and legislative history and applying relevant case precedent.[8]

During the past 30 years, this Court has construed Title VII in dozens of decisions with regard to shifting burdens of proof, theories of liability (*e.g.*, disparate impact and treatment, mixed motive factors, hostile environment), potential defenses (*e.g.*, bona fide occupational qualification, business necessity, after-acquired evidence) and available remedies (*e.g.*, back pay, front pay, injunctive relief, compensatory and punitive damages and attorneys' fees). Congress itself has revisited the statute several times, often in response to those judicial decisions. Yet as Desiderio's complaint alleges, securities industry arbitrators are, for the most part, legally-untrained former securities industry executives (¶ 29f), who are told that they have no obligation to follow the law, whose decisions are virtually unreviewable for statutory error, and who are advised not to state the rationale for their awards in order to further insulate their decisions from any meaningful judicial review. (¶ 29e)

The right to have the law enforced correctly — especially a doctrinally complex law like Title VII — is the ultimate substantive right. In the securities arbitration forum, however, a Title VII claimant's right to have the law enforced according to its terms is impermissibly transformed from a matter of statutory *entitlement* to a matter of arbitral *discretion*. Title VII requires more. A policy that encourages decisionmakers to make decisions without being bound by the language or judicial

8. *See Alexander v. Gardner-Denver Co.*, *supra*, 415 U.S. at 57 (federal judges have "primary responsibility" for resolving statutory or constitutional issues, and their expertise has been "especially necessary with respect to Title VII, whose broad language frequently can be given meaning only by reference to public law concepts"). *Accord*, *Kremer v. Chemical Constr. Corp.*, 456 U.S. 461, 468 (1982) ("federal courts were entrusted with ultimate enforcement responsibility" under Title VII); *New York Gaslight Club, Inc. v. Carey*, 447 U.S. 54, 64 (1980) ("Of course, the 'ultimate authority' to secure compliance with Title VII resides in the federal courts").

constructions of the statute deprives statutory claimants of rights and protections provided by the law. *See Cole*, *supra*, 105 F.3d at 1468, 1482; *Paladino v. Avnet Computer Technologies, Inc.*, *supra*, 134 F.3d at 1062 (separate opinion of Cox, J., joined by Tjoflat, J.).

b. Securities Industry Arbitrators Regularly Assess Prevailing Plaintiffs With Forum Fees and Often Fail to Follow Title VII's Fee Shifting Requirements

Second, although Congress in Title VII sought to encourage the vindication of statutory rights by shifting a prevailing plaintiff's reasonable attorneys' fees and costs to the losing defendant (*see* 42 U.S.C. § 2000e-5(k)), Desiderio's complaint alleges (based on empirical research into post-*Gilmer* arbitration awards) that securities arbitrators *often* violate Title VII's core principles: (1) by refusing to award statutory attorneys' fees to prevailing plaintiffs (¶ 29k); and (2) by charging them thousands of dollars in forum fees, which increase with the complexity of the case and which serve as a substantial economic deterrent for workers considering whether to seek redress for their employer's legal violations. (¶ 29j)

By so skewing the economic balance that Congress deemed essential to federal anti-discrimination policy, securities industry arbitration undermines Congress' carefully-crafted statutory standards and improperly chills the exercise of protected statutory rights. As Congress itself noted in the 1991 Civil Rights Act legislative history, practices that "limit [a prevailing plaintiff's] recovery of attorneys' fees, other fees, and other costs of litigation under Title VII . . . frustrate[s] the intent of Congress to protect the public interest by eliminating employment discrimination and to ensure that victims of such discrimination be made whole for the losses they have suffered." H.R. Rep. No. 40(II) at 30, 102nd Cong., 1st Sess. (1991), *reprinted in* 1991 U.S.C.C.A.N. at 723; *see also Cole*, 105 F.3d at 1468.

Title VII and other similar statutes serve important public policies of compensation and deterrence. Their broad remedial provisions are designed not only to make victims of discrimination whole, but to serve as a "spur or catalyst" to induce employers to "endeavor to eliminate, so far as possible, the last vestiges" of discrimination. *Albemarle Paper Co. v. Moody*, 422 U.S. 405, 417-18 (1975). These goals can only be achieved if the process for resolving statutory employment claims contains the burden-shifting provisions that Congress deemed central to effective enforcement of anti-discrimination laws. Those protections are *not* provided in the securities industry's current mandatory arbitration scheme, which supplants court adjudication without providing the essential safeguards guaranteed by law.

The potential imposition of substantial "forum fees" on Title VII plaintiffs provides a compelling reason, by itself, for ruling that Desiderio cannot be required to arbitrate in the securities industry forum. As the D.C. Circuit explained in *Cole* (a case that arose outside the securities context, in which the court construed an ambiguous clause in an arbitration agreement as *not* requiring the payment of forum fees, in order to avoid having to invalidate that clause):

> [T]his case raises an issue not directly presented in *Gilmer* or any other Supreme Court case to date: can an employer require an employee to arbitrate all disputes and also require the employee to pay all or part of the arbitrators' fees? We hold that it cannot. . . .
>
> In our view, *an employee can never be required, as a condition of employment, to pay an arbitrator's compensation in order to secure the resolution of statutory claims under Title VII* (any more than an employee can be made to pay a judge's salary). If there is any risk that an arbitration agreement can be construed to require this result, this would surely

> deter the bringing of arbitration and constitute a *de facto* forfeiture of the employee's statutory rights. (emphasis added)

Id. at 1468 (footnote omitted).

c. The Unavailability of Meaningful Judicial Review Increases the Risk that the Securities Industry Arbitration Will Not Adequately Protect Statutory Rights

Third, the lack of meaningful judicial oversight exacerbates the problems of securities industry arbitrator selection, training and decision-making. When statutory rights are at stake, judicial review should be "sufficiently rigorous to ensure that arbitrators have properly interpreted and applied statutory law." *Cole*, 105 F.3d at 1487. But arbitration awards, unlike judicial decisions, are not reviewable for statutory error and cannot be reversed on the ground that the arbitrators did not correctly apply statutory principles. Unless the arbitrator's award shows on its face that the arbitrator *knew* the law and *deliberately* ignored it, a court cannot overturn that award.[9]

Judicial review could provide some check on arbitral error if the arbitrators included findings of fact, conclusions of law, or a discussion of their reasoning in their awards (a level of detail that the Court in *Gilmer* apparently assumed would be provided by NYSE arbitrators). But as the Desiderio complaint alleges, NASD's training manual expressly discourages arbitrators from providing written analyses, precisely to avoid judicial review, thereby encouraging those arbitrators to rest their rulings on their innate sense of what is "fair", rather than on what the law dictates. (¶ 29c)

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9. *See, e.g.*, 9 U.S.C. § 10; *Prudential-Bache Secs., Inc. v. Tanner*, 72 F.3d 234, 239 n.6 (1st Cir. 1995); *DiRussa v. Dean Witter Reynolds, Inc.*, *supra*, 121 F.3d at 821-22 (failure to award attorneys' fees not grounds for overturning award where arbitrator was not aware that statute required fee-shifting).

d. A Circuit Conflict Exists With Respect to Mandatory Arbitration Procedures Permitting the Imposition of Substantial Filing and Forum Fees

There is a conflict among the Circuits as to the adequacy of mandatory arbitration schemes that routinely impose substantial filing and forum fees. Certiorari should be granted in this case to resolve the conflict.

The Ninth, Tenth, Eleventh and District of Columbia Circuits have recently ruled that employees may not be required to pay significant fees to vindicate their statutory rights under Title VII. *See Shankle v. B-G Maintenance Management*, 163 F.3d 1230 (10th Cir. 1999); *Paladino v. Avnet Comp. Techs., Inc.*, 134 F.3d 1054 (11th Cir. 1998); *Cole v. Burns Int'l Sec. Svcs.*, 105 F.3d 1465 (D.C. Cir. 1997). *Cf. Duffield v. Robertson, Stephens & Co.*, 144 F.3d 1182 (9th Cir.), *cert. denied*, __ U.S. __, 119 S. Ct. 465 (1998). As the Tenth Circuit explained, in striking down a mandatory arbitration agreement that required an employee to pay expensive fees:

> The Agreement thus placed Mr. Shankle between the proverbial rock and a hard place — it prohibited the use of the judicial forum, where a litigant is not required to pay for a judge's services, and the prohibitive cost substantially limited use of the arbitral forum. *See Cole [v. Burns Int'l Sec. Serv.*, 105 F.3d 1465, 1484 (D.C. Cir. 1997)] (concluding employees would be unable to pursue statutory claims if required to pay for arbitrator fees in addition to the administrative costs and attorneys fees, which accompany both arbitration and litigation). Essentially B-G Maintenance required Mr. Shankle to agree to mandatory arbitration as a term of continued employment, yet failed to provide an accessible forum in which he could resolve his statutory rights. Such a result clearly undermines

> the remedial and deterrent functions of the federal anti-discrimination laws. [Citations omitted]. *Shankle*, 163 F.3d at 1235.

Conversely, the First Circuit in *Rosenberg v. Merrill Lynch Pierce Fenner & Smith, Inc.*, 170 F.3d 1 (1st Cir. 1999), rejected an employee's argument that mandatory arbitration is an impermissible condition of employment if it imposes forum fees. Similarly, the Seventh Circuit in *Koveleskie v. SBC Capital Markets*, 167 F.3d 361 (7th Cir. 1999), *cert. denied*, __ U.S. __, 120 S. Ct. 44 (1999), rejected the employee's argument that the arbitral forum failed to protect her statutory rights because of the imposition of forum fees. Adopting *Rosenberg's* reasoning, the *Koveleskie* court stated "[I]t does not appear to be the usual situation that a plaintiff is asked to bear forum fees . . ." and ". . . if unreasonable fees were to be imposed on a particular employee, the argument that this was inconsistent with the 1991 Act could be presented by the employee to the reviewing court." *Id.* at 366.[10] The Third Circuit in *Seus v. John Nuveen & Co.*, 146 F.3d 175 (3d Cir. 1998), *cert. denied*, __ U.S. __, 119 S. Ct. 1028 (1999), also upheld a compulsory arbitration scheme that permitted the imposition of forum fees on the claimant.

The holdings of the Second Circuit in this case and the First, Third and Seventh Circuits reflect an indifference to the dilemma confronting employees who must decide whether to submit claims to an arbitral forum, thereby risking exposure to untold forum fees, or to forego vindicating their civil rights. Whether these fees ultimately are assessed in most cases is

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10. Both the First and Seventh Circuits cite *Cole* for the patently incorrect proposition that the securities industry arbitration system does not require employees to pay forum fees. *Cole*, 105 F.3d at 1483; *Rosenberg*, 170 F.3d at 44-46; *Koveleskie*, 167 F.3d at 366. Petitioner has explicitly pleaded otherwise. See also NASD Code of Arbitration Procedure Sections 44(b) and (c) (providing for payment of forum fees and empowering arbitrators to determine the amount of such fees chargeable to each party).

beside the point; the possibility that such fees could be assessed chills claim filing. As the Tenth Circuit held in *Shankle*, the absence of an affordable process renders the arbitral forum inadequate and undermines the remedial and deterrent functions of the federal and state anti-discrimination laws.

By making it difficult for the aggrieved employee intelligently to weigh the risks of litigation, the uncertainty as to whether the employee will be assessed forum costs, even if she prevails, necessarily has a chilling effect on the filing of statutory claims. Some unemployed claimants, unable to assume the financial risk entailed in invoking such arbitration, will simply forego seeking to vindicate their civil rights, thereby undermining the Congressional intent to eradicate discrimination. The Second Circuit in affirming the dismissal of Desiderio's complaint has sanctioned such procedures, notwithstanding that NASD arbitrators commonly impose onerous and exorbitant forum fees on prevailing employee litigants. (¶ 29j)

B. The Circuit Conflict Regarding State Action and the Doctrine of Unconstitutional Conditions

The doctrine of unconstitutional conditions prohibits the government from conditioning a worker's employment upon a waiver of that worker's constitutional rights. This doctrine has long put to rest "Justice Holmes' famous dictum that a policeman 'may have a constitutional right to talk politics, but he has no constitutional right to be a policeman.' " *Bd. of Cty. Com'rs v. Umbehr*, 518 U.S. 668, 674 (1996), *quoting McAuliffe v. Mayor of New Bedford*, 155 Mass. 216, 220, 29 N.E. 517 (1892).[11]

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11. *See also Greene v. McElroy*, 360 U.S. 474 (1959) (independent contractors); *United States v. Robel*, 389 U.S. 258 (1967); *O'Hare Truck Services, Inc. v. City of Northlake*, 518 U.S. 712 (1996); *Barron v. Burnside*, 121 U.S. 186 (1887) (state may not condition corporation's license to do business upon waiver of Article III right to sue in federal court); *Herndon v. Chicago, Rock Island & Pacific Railway Co.*, 218 U.S. 135 (1910) (same); *see generally* K. Sullivan, *Unconstitutional Conditions*, 102 Harv. L. Rev. 1413 (1989); R. Reuben, *Public Justice:*

(Cont'd)

The unconstitutional conditions issue was not presented in *Gilmer*. Nor has the Court ever considered that issue with respect to mandatory securities industry arbitration of employment claims.

Desiderio argued below that the federal government, through statute, SEC regulation, and SEC oversight, is ultimately responsible for the requirement of mandatory securities industry arbitration that cost petitioner her job. She further argued that this requirement imposed a non-negotiable condition upon her employment that unconstitutionally deprived her of the right under Article III of the Constitution not to be forced by the federal government to adjudicate her employment claims in a non-Article III forum, her Seventh Amendment right to a jury trial, and her Fifth Amendment rights to due process and equal protection. Certiorari should be granted to review these claims, which have also split the circuits, as an alternative ground for reversing the Second Circuit.

1. The State Action Inquiry and Determination

The "state action" inquiry ultimately turns on whether there is "a sufficiently close nexus between the State and the challenged action" such that "the alleged infringement of [constitutional] rights [is] fairly attributable to the State." *Lebron v. Natl. R.R. Passenger Corp.*, 513 U.S. 374, 408 (1995) (O'Connor, J., dissenting), quoting from *Jackson v. Metropolitan Edison Co.*, 419 U.S. 345, 351 (1974), and *Rendell-Baker v. Kohn*, 457 U.S. 830, 838 (1982). This Court has acknowledged that the "state action" doctrine has confused the lower courts and that it requires further development by this Court. "It is fair to say that 'our cases deciding when private action might be deemed that of the state have not been a model of consistency.' " *Lebron*, 513 U.S. at 378, quoting *Edmondson v. Leesville Concrete Co.*, 500 U.S. 614, 632 (1991).

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Toward a State Action Theory of Alternative Dispute Resolution, 85 Cal. L. Rev. 3 (1997); J. Ware, *Employment Arbitration and Voluntary Consent*, 25 Hofstra L. Rev. 83 (1996).

2. The Conflict in the Circuits With Respect to Determining State Action

The Second Circuit rejected Desiderio's unconstitutional conditions argument after concluding that requisite state action was absent with respect to the NASD's imposition of mandatory securities industry arbitration as a condition of employment. This holding was erroneous, and squarely conflicts with decisions of the Seventh, Ninth, and District of Columbia Circuits. Under those decisions, the SEC's promulgation of 17 C.F.R. § 240.15b7-1 in May 1993 is sufficient, standing alone, to trigger constitutional scrutiny of mandatory securities industry arbitration for traders, like petitioner, hired after that date. The SEC's requirement that traders be registered with an exchange as a condition of trading securities placed the government's imprimatur — indeed, its mandate — upon the exchanges' rules, including their mandatory arbitration rules.

In *Blount v. SEC*, 61 F.3d 938 (D.C. Cir. 1995), *cert. denied*, 517 U.S. 1119 (1996), the D.C. Circuit considered a constitutional challenge to a rule, promulgated by the Municipal Securities Rulemaking Board ("MSRB") and approved by the SEC, that regulated political contributions by municipal securities broker-dealers. 61 F.3d at 939. Intervenor MSRB defended on the ground that it was a private organization whose rules were not subject to constitutional scrutiny. *Id.* at 941. The D.C. Circuit rejected this argument, concluding that even if the MSRB were a private organization, enforcement of its rules would constitute state action because, under federal law, all municipal securities broker-dealers, as a condition of employment in the industry, were required to register with the MSRB and to obey its SEC-approved rules. *Id.* Because of the registration requirement, those MSRB rules "operat[ed] not as a private compact among brokers and dealers but as federal law." *Id.*

Similarly, in *R.J. O'Brien & Assoc., Inc. v. Pipkin*, 64 F.3d 257 (7th Cir. 1995), the Seventh Circuit found state action in the mandatory arbitration rules of the National Futures

Association ("NFA"), a private organization with which commodities futures brokers were required to register as a condition of trading commodities futures. 64 F.3d at 259. Despite the private nature of the NFA, the Seventh Circuit found state action because federal law required the broker to register with the NFA, and thus to comply with its rules, including its mandatory arbitration rules. *Id.* at 262.

In *Duffield v. Robertson, Stephens & Company*, *supra*, a case that also raised an unconstitutional conditions challenge to the securities industry's mandatory arbitration rules, the Ninth Circuit held that state action was not present with respect to a plaintiff who was compelled to sign a Form U-4 before 1993, *but that state action would exist for securities traders, like petitioner Desiderio, who were hired and challenged their compelled registration after that date*. The Ninth Circuit explained:

> [In] 1993, . . . the Securities and Exchange Commission (SEC) adopted a regulation that required all broker-dealers to be registered with at least one of the securities organizations of which Duffield's firm was a member — i.e., the NASD and the NYSE — before effecting any securities transaction. *See* 17 C.F.R. § 240.15b7-1 (adopted May 11, 1993). That registration regulation, like the SEC's registration regulation at issue in *Blount v. SEC*, 61 F.3d 938 (D.C. Cir. 1995), *cert. denied*, 116 S.Ct. 1351 (1996), "operates not as a private compact among brokers and dealers but as federal law." *Id.* at 941. Hence, to borrow *Blount's* reasoning, as a government-mandated "condition to any participation in a . . . securities career," the current requirement that new employees register with a national securities exchange "constitutes government action of the purest sort." *Id.*

Under these authorities, rejected by the Second Circuit in the present case, the SEC's promulgation of 17 C.F.R. § 240.15b7-1 in May 1993 should have been sufficient to trigger constitutional scrutiny of mandatory securities industry arbitration for traders hired after that date.

3. The SEC's Repeated Exercise of its Oversight Authority With Respect to the NASD's Mandatory Employment Arbitration Rules Establishes State Action

State action exists where the government "has provided such significant encouragement, either overt or covert, that the [private party's] choice must in law be deemed to be that of the State." *Blum v. Yaretsky*, 457 U.S. 991, 1004 (1982); *see, e.g., Skinner v. Railway Labor Exec. Ass'n*, 489 U.S. 602, 615-16 (1989) (allowing a constitutional challenge to a private railroad's drug-testing of employees pursuant to federal regulations that authorized but did not compel drug-testing, because federal regulation of discretionary procedures demonstrated that "the Government did more than adopt a passive position toward the underlying private conduct").[12] Here the federal government went well beyond compelling the exchanges to enforce their registration and mandatory arbitration rules against Desiderio. Long prior to promulgating its 1993 regulation, the SEC was actively involved in formulating those mandatory arbitration

12. *See also Public Utilities Comm. v. Pollak*, 343 U.S. 451, 462 (1952) (private transit company's policy of playing music through bus loudspeakers constitutes state action because the policy was reviewed and approved by government officials). Although state action was not found in *Blum v. Yaretsky*, 457 U.S. 991, that was because the challenged decisions were made by private doctors pursuant to their independent exercise of professional judgment, free from government influence. *See, e.g.*, 457 U.S. at 1006 ("the physicians, and not the forms, make the decision about whether patient's care is medically necessary. a physician can authorize a patient's admission to a nursing facility despite a 'low' score on the form"); *id.* at 1006, n.16 (the physicians "render medical judgments concerning the patient's health needs that the State does not prescribe and for which it is not responsible").

rules and has for many years closely overseen their implementation. The SEC has repeatedly exercised its oversight authority with respect to the exchanges' mandatory employment arbitration rules, just as it did with respect to the NASD's recent rule change and with the securities industry's Form U-4.[13]

The SEC staff has also conducted a longstanding dialogue with the exchanges about those arbitration rules and procedures, resulting in a consensus between industry and the SEC approval. Many of those rules, including several that are at the heart of Desiderio's due process challenge to the adequacy of mandatory securities industry arbitration, were initially proposed by the SEC itself. Indeed the SEC was the initial source for the Form U-4. Cf. *Intercontinental Indus., Inc. v. Amer. Stock Exchange*, 452 F.2d 935, 941 & n.9 (5th Cir. 1971), *cert. denied*, 409 U.S. 842 (1972) (SEC's control over NYSE rulemaking subjects those rules to due process review).[14] These facts make this even

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13. The SEC on June 22, 1998 approved sweeping amendments to the NASD's arbitration rules, exempting all employment discrimination and sexual harassment claims from that exchange's mandatory securities industry arbitration requirement effective January 1, 1999. *See* SEC Order Granting Approval To Proposed Rule Change Relating to the Arbitration of Employment Discrimination Claims, SR-NASD-97-77, SEC Release No. 34-40109 (June 22, 1998). The SEC then called upon the NYSE and other exchanges to submit similar amendments to their mandatory arbitration rules for SEC approval.

14. *See, e.g.*, SEC Release No. 34-17373, 1980 LEXIS 100 (Dec. 17, 1980) (Form U-4); SEC Release No. 34-11424, 1975 LEXIS 1592 (May 16, 1975) (same); SEC Release No. 34-26805, 1989 SEC LEXIS 843 (May 10, 1989) at 4 (during the past two decades, "[t]he majority of the proposals to amend the [exchanges' arbitration] rules were . . . in response to the . . . Commission letters"); *id.* at 3-5, 7, 16, 22, 31, 32, 44 n.51, 51 n.59 (describing the SEC's ongoing series of letters to the exchanges, communicated through Securities Industry Conference on Arbitration, that presented the SEC's views on the exchanges' arbitration procedures, "requested [that the exchanges] amend their rules" to conform to the SEC's views, and resulted in a series of proposed rule changes that were "develop[ed] in response to

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a stronger "state action" case than *Blount* or *R.J. O'Brien*, because nothing in those cases suggests that the government was actively involved with the *substance* of the rules being enforced.[15]

The Securities and Exchange Act also prohibited the securities exchanges from modifying those rules and procedures without the SEC's approval, while that agency has unilateral power to change those rules at any time. The resulting scheme is thus "fairly attributable" to the state within the meaning of this Court's state action authorities. *See, e.g., Lugar v. Edmundson Oil Co.*, 457 U.S. 922, 937 (1982).

4. As a State Actor, the NASD Mandatory Arbitration Rules Imposed an Unconstitutional Condition on Desiderio's Employment

Once the "state action" threshold is crossed, it necessarily follows that the NASD's mandatory arbitration rules imposed an unconstitutional, and hence unenforceable, condition of employment on Desiderio depriving her of constitutional rights.

Article III of the Constitution vests the "judicial Power of the United States" in courts whose judges have lifetime tenure and salary protection. Under this Court's precedents, the federal

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the Commission's letters"). *See also* SEC Release No. 34-26805, 1989 SEC LEXIS 843 (May 10, 1989) (approving detailed changes to arbitration procedures, including fee, discovery, and panel selection matters, and rejecting public comments requesting, *inter alia*, that arbitrators be required to state the reasons for their decisions).

15. These facts also distinguish this case from *Jackson v. Metropolitan Edison Co.*, 419 U.S. 345 (1974), in which a state agency merely did not act to disapprove a tariff filed by a utility company. There was no evidence in *Jackson* that the agency was aware of the provision of the tariff being challenged, much less that the agency had any role in formulating, or even consulting with the utility company about, that provision. We also note that *Jackson* involved a business corporation, not a regulatory organization deputized by the federal government to help police the securities industry.

government may not consign parties to the jurisdiction of a non-Article III forum to resolve essentially private, state-law claims, at least not without the parties' consent. *See Commodity Futures Trading Commission v. Schor*, 478 U.S. 833, 848-50 (1986); *Thomas v. Union Carbide Agricultural Products Co.*, 473 U.S. 568, 584 (1985) ("Congress may not vest in a non-Article III court the power to adjudicate, render final judgment, and issue binding orders in a traditional contract action, without *consent* of the parties. . . ." (emphasis supplied)); *Northern Pipeline Construction Co. v. Marathon Pipe Line Co.*, 458 U.S. 50, 84 (1982) (plurality opinion). Here Desiderio insisted in preserving her rights, and refused to waive her right to an Article III court on future claims. This case is therefore unlike *CFTC v. Schor*, where plaintiffs were deemed to have consented to have a non-Article III tribunal hear counterclaims against them because they submitted their affirmative claims to the same non-Article III tribunal. Desiderio strenuously argued from the outset that she should be permitted to litigate her claims in court.

The Seventh Amendment precludes the federal government from depriving litigants of the right to a trial by jury on claims that "involve[] rights and remedies of the sort typically enforced in an action at law." *Curtis v. Loether*, 415 U.S. 189, 195 (1974). Desiderio's state common law tort and contract claims unquestionably "involve[] rights and remedies of [that] sort." While the right to a jury may be waivable, Desiderio's complaint against the NASD contains an express demand for a jury trial. Again, the unconstitutional conditions doctrine compels the conclusion that the imposition of such a mandatory surrender of a constitutional right absent a voluntary waiver is an unconstitutional condition that impermissibly compromises Seventh Amendment rights.

With respect to the Fifth Amendment right to due process, mandatory securities industry arbitration denies Desiderio the right, enjoyed by workers in all other industries,

to have her statutory claims decided by a tribunal that is required to apply pertinent statutes and case precedents. Desiderio's complaint, (¶ 29) pleads *inter alia*: that securities industry arbitrators are expressly instructed that they may ignore the law in favor of their own sense of "fairness"; that they do in fact ignore the law, such as by denying attorney's fees to prevailing plaintiffs who have a statutory entitlement to them and by imposing steep "forum fees" of tens of thousands of dollars upon litigants including prevailing plaintiffs; that empirical studies show that securities industry arbitrators are more likely than courts to rule for employers on employment claims and to award lower damages when a plaintiff does prevail; and that securities industry arbitrators are instructed not to provide reasoning for their decisions (and do not, in fact, provide reasoning in their largely staff-written arbitration awards) so as to make meaningful judicial review of the substance of their decisions close to impossible.[16]

The ultimate due process right is the right to have one's claim resolved in accordance with the governing law. Although a plaintiff may voluntarily agree to have a statutory dispute resolved under inadequate procedures, the government cannot compel a plaintiff to submit to such procedures as a condition of retaining or obtaining employment in her desired profession.

C. The Court Should Resolve this Circuit Split Because it is Vitally Important to Employers, Employees, and Courts Nationwide

The issue of arbitrability of federal and state statutory antidiscrimination claims (and indeed of claims arising under the whole array of legislation enacted to protect workers) is of immediate and vital concern to employers, employees, and the federal and state courts throughout the country.

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16. *See Halligan v. Piper Jaffray, Inc.*, 148 F.3d 197 (2d Cir. 1998), *cert. denied*, __ U.S. __, 119 S. Ct. 1286 (1999).

Although this case arose in the securities industry, its impact is far broader. The question considered below affects every agreement between employers and employees to arbitrate statutory employment disputes, including Title VII claims, in nearly every sector of the economy.[17]

CONCLUSION

For the foregoing reasons, the Petition for a Writ of Certiorari should be granted.

Respectfully submitted,

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17. Since this Court's decision in *Gilmer*, a growing number of employers have instituted mandatory arbitration procedures for statutory employment disputes. A 1994 General Accounting Office survey of private businesses found that approximately 10% of employers had mandatory arbitration procedures in place for discrimination complaints. U.S. General Accounting Office, *Employment Discrimination: Most Private-Sector Employers Use Alternative Dispute Resolution* at 7 (GAO/HEHS-95-150). It is safe to surmise that the percentage of employers adopting such procedures has dramatically increased in the past six years.

APPENDIX

APPENDIX A — OPINION AND ORDER OF THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT DATED AND FILED SEPTEMBER 22, 1999

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

August Term, 1998

(Argued December 7, 1998 Decided SEP 22 1999)

Docket No. 98-6100

SUSAN A. DESIDERIO,

Plaintiff-Appellant,

v.

NATIONAL ASSOCIATION OF
SECURITIES DEALERS, INC.,

Defendant-Appellee.

Before:

KEARSE, CARDAMONE, and STRAUB,
Circuit Judges

* * *

Appendix A

CARDAMONE, *Circuit Judge*:

Plaintiff, Susan A. Desiderio, received an offer of employment from Florida's Suntrust Bank (Suntrust or bank) to become a securities broker. Her employment was conditioned on registration with defendant National Association of Securities Dealers, Inc. (NASD). To register with the NASD, Desiderio was asked to sign Form U-4 that contained a provision making all employment related disputes subject to arbitration. Desiderio said she would sign the form only if the mandatory arbitration provision was stricken from it. When the NASD refused to accept an altered form, the bank's offer of employment to plaintiff was revoked.

In her complaint, Desiderio asserts that the mandatory arbitration provision in Form U-4 violates her statutory rights under Title VII, 42 U.S.C. §§ 2000e to e-17, her constitutional rights under the Fifth Amendment Due Process Clause to an Article III judicial forum, and her right to a jury trial under the Seventh Amendment. She seeks a declaratory judgment invalidating the mandatory arbitration provision in Form U-4, and also asks for compensatory damages through her pendent state law tort claims.

BACKGROUND

Defendant NASD is a self-regulatory private corporation registered with the Securities and Exchange Commission (SEC) as a national securities association. As an integral part of a comprehensive system of federal regulation of the securities industry, the NASD regulates the over-the-counter

securities market, which includes securities firms and registered representatives who buy and sell over-the-counter-securities. Its authority is exercised under the close supervision of the SEC, which must approve all the NASD's rules and regulations. Among the rules that have been expressly approved by the SEC is the Form U-4 registration form. That form — the subject of this litigation — incorporates a provision for compulsory arbitration of all disputes between a securities representative and her employer, when required by the rules of the self-regulatory organization with which the securities representative seeks to become registered. Under NASD rules, all employees are compelled to arbitrate any employment-related dispute. In order to work in the securities industry, the SEC requires a securities broker to be registered with at least one self-regulatory organization, *see* 17 C.F.R. § 240.15b7-1 (1998), and registration in such organization entails signing Form U-4.

The NASD operates an arbitration forum for the purpose of resolving disputes between securities brokers and their employers. Its Code of Arbitration Procedure regulates the composition of the arbitration panel, provides for the disclosure of information by arbitrators concerning potential conflicts of interest, and also provides for the subsequent removal of an arbitrator by means of a challenge. Under the procedure an arbitration award must be in writing.

On March 18, 1996 Desiderio, as noted, was hired as a registered representative by Suntrust, conditioned upon her signing a Form U-4 as required by both state and federal law. She signed the Form U-4, but struck out the mandatory

arbitration provision. Suntrust had no objection to Desiderio's modification of the form. But NASD did. An employee of NASD, in a telephone conversation, allegedly advised Suntrust that an altered Form U-4 was unacceptable for registration. Plaintiff refused to execute an unaltered one. Because Desiderio could not become registered, Suntrust revoked its offer of employment. The altered Form U-4 was never submitted to the NASD.

Plaintiff subsequently filed a complaint instituting the present action on January 15, 1997, naming both the NASD and the SEC as defendants. In a judgment entered on April 23, 1998, the United States District Court for the Southern District of New York (Leisure, J.) granted defendants' motions to dismiss plaintiff's complaint for failure to state a claim pursuant to Rules 12(b)(6) and 12(b)(1) of the Federal Rules of Civil Procedure. Plaintiff appeals from that judgment. Her appeal against the SEC was stipulated to be withdrawn, leaving the NASD as the only appellee. We affirm.

DISCUSSION

Mootness & Ripeness

We dispose first of the threshold question of whether this case is moot. On June 22, 1998 while this case was pending, the SEC approved a proposed rule change offered by the NASD that abolishes mandatory NASD arbitration of statutory employment discrimination claims. *See* Self Regulatory Organizations; National Association of Securities Dealers, Inc.; Order Granting Approval to Proposed Rule

Appendix A

Change Relating to the Arbitration of Employment Discrimination Claims, 63 Fed. Reg. 35299, 35303 (1998) (Order Granting Approval). The rule change became effective on January 1, 1999. *See id.* As a result, the NASD argues that many of Desiderio's claims have become moot.

As a general rule, in a case involving an allegation that defendant has engaged in illegal activity, a court's power to hear and decide the matter is not terminated when defendant voluntarily ceases its illegal conduct. That is, such cessation does not necessarily make a case moot. *See County of Los Angeles v. Davis*, 440 U.S. 625, 631 (1979) (citing *United States v. W. T. Grant Co.*, 345 U.S. 629, 632 (1953)); *New York State Nat'l Org. for Women v. Terry*, 159 F.3d 86, 91-92 (2d Cir. 1998), *cert. denied sub nom. Pearson v. Planned Parenthood Margaret Sanger Clinic*, 67 U.S.L.W. 3570, 3754, 3756 (U.S. June 14, 1999) (No. 98-1435). A case may nevertheless be moot if the defendant can demonstrate that: "(1) it can be said with assurance that there is no reasonable expectation . . . that the alleged violation will recur, . . . and (2) interim relief or events have completely and irrevocably eradicated the effects of the alleged violation." *Davis*, 440 U.S. at 631. The burden of demonstrating mootness "is a heavy one." *Id.*; *W. T. Grant Co.*, 345 U.S. at 633; *Terry*, 159 F.3d at 91.

The NASD amended its rules voluntarily. *See* Order Granting Approval, 63 Fed. Reg. 35299, 35300. In light of proof that the rule change was partially prompted by political concerns such as letters from members of Congress, *see id.* at 35300, the NASD has not met its burden of showing that there is no reasonable expectation that this rule will ever be

reinstated, *see Davis*, 440 U.S. at 631. Securities firms who are members of the NASD may have an interest in lobbying to reimpose the mandatory arbitration rule with respect to statutory discrimination claims, and there is no evidence that such lobbying would be ineffective. In addition, interim relief and events have not completely and irrevocably eradicated the effects of the alleged violation on plaintiff, *see id.* As approved by the SEC, the rule change only applies to claims filed on or after January 1, 1999. *See* Order Granting Approval, 63 Fed. Reg. at 35301. As a result, plaintiffs with currently pending statutory discrimination claims that were filed before January 1, 1999 are still compelled to arbitrate. Thus, this case presents a situation where the "public interest in having the legality of the practices settled, militates against a mootness conclusion." *W. T. Grant Co.*, 345 U.S. at 632.

The NASD further urges that Desiderio's claims are not ripe because she never actually submitted her Form U-4 to the NASD. However, "[w]e will not require . . . a futile gesture as a prerequisite for adjudication in federal court." *Williams v. Lambert*, 46 F.3d 1275, 1280 (2d Cir. 1995) (claim was ripe because attempt to modify agreement would be futile); *cf. International Bhd. of Teamsters v. United States*, 431 U.S. 324, 365-66 (1977) (person who never applied for job is entitled to retroactive seniority if applying would have been futile because of discriminatory hiring practices). It would have been futile for Desiderio to submit an altered Form U-4 after being told that the NASD advised Suntrust that emendation of Form U-4 would not be accepted for registration purposes.

Appendix A

Standard of Review

We review dismissal of a cause of action under the Federal Rules of Civil Procedure 12(b)(6) *de novo*. *See Jaghory v. New York State Dep't of Educ.*, 131 F.3d 326, 329 (2d Cir. 1997). Under *de novo* review, we accept all of plaintiff's factual allegations in the complaint as true and draw inferences from those allegations in the light most favorable to the plaintiff. We will not affirm the dismissal of a complaint unless "it appears beyond doubt, even when the complaint is liberally construed, that the plaintiff can prove no set of facts which would entitle him to relief." *Id.*

I Statutory Rights Under Title VII

A. *Views of Other Circuits*

Whether a pre-dispute agreement requiring compulsory arbitration, such as Form U-4, is enforceable with regard to Title VII claims is an issue that has divided the circuits and is one of first impression in this Court. Practically every circuit that has addressed the question has held that the arbitration clause in Form U-4 validly applies to Title VII claims. *See Rosenberg v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 170 F.3d 1, 7 (1st Cir. 1999); *Seus v. John Nuveen & Co.*, 146 F.3d 175, 182 (3d Cir. 1998), *cert. denied*, 119 S. Ct. 1028 (1999); *Austin v. Owens-Brockway Glass Container, Inc.*, 78 F.3d 875, 882 (4th Cir.), *cert. denied*, 519 U.S. 980 (1996); *Alford v. Dean Witter Reynolds, Inc.*, 939 F.2d 229, 230 (5th Cir. 1991); *Willis v. Dean Witter Reynolds, Inc.*, 948 F.2d 305, 307 (6th Cir. 1991); *Koveleskie v. SBC Capital Mkts., Inc.*, 167 F.3d 361, 365 (7th Cir.),

petition for cert. filed, 67 U.S.L.W. 3707 (U.S. May 5, 1999) (No. 98-1778); *Patterson v. Tenet Healthcare, Inc.*, 113 F.3d 832, 837 (8th Cir. 1997); *Metz v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 39 F.3d 1482, 1487 (10th Cir. 1994); *Bender v. A.G. Edwards & Sons, Inc.*, 971 F.2d 698, 700 (11th Cir. 1992); *Cole v. Burns Int'l Sec. Servs.*, 105 F.3d 1465, 1482-83 (D.C. Cir. 1997).

In a notable exception to this unanimity, the Ninth Circuit has ruled that the Form U-4 compulsory arbitration clause is unenforceable with regard to Title VII claims. *See Duffield v. Robertson Stephens & Co.*, 144 F.3d 1182, 1190 (9th Cir.), *cert. denied*, 119 S. Ct. 445, 465 (1998). Further, the EEOC has issued a policy statement that supports the conclusion found in *Duffield*. *See* EEOC, Notice No. 915.002, Policy Statement on Mandatory Binding Arbitration of Employment Discrimination Disputes as a Condition of Employment (1997), *available in* LEXIS, 2NDARY Library, EEOMAN FILE.

The circuit conflict stems from varying interpretations of *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20 (1991). In *Gilmer*, the Supreme Court held that employees could be required under Form U-4 and New York Stock Exchange Rule 347 to arbitrate age discrimination claims brought under the Age Discrimination in Employment Act (ADEA). *Id.* at 23. Most circuits have found the analytical framework used in *Gilmer* with respect to the ADEA applies to Title VII as well. Thus, we proceed to examine *Gilmer's* application to Title VII claims.

Appendix A

B. *Applicability of Gilmer and the FAA*

The Civil Rights Act of 1991 (Act) added a provision on arbitration to Title VII stating that "[w]here appropriate and to the extent authorized by law, the use of . . . arbitration[ ] is encouraged" to resolve Title VII claims. Pub. L. No. 102-166, § 118, 105 Stat. 1071, 1081 (§ 118), *reprinted in* 42 U.S.C. § 1981 app. at 509 (1994). We agree with the view of the majority of circuits that the phrase "to the extent authorized by law" is on its face a clear and unambiguous reference to "current law." *See, e.g., Seus*, 146 F.3d at 183. Hence, as current law, both *Gilmer* and the Federal Arbitration Act (FAA) apply to our analysis of § 118.

In contrast, the Ninth Circuit in *Duffield* suggested that the phrase "to the extent authorized by law" refers not to current law as stated in *Gilmer* and the FAA, but instead refers to a previously relevant case, *Alexander v. Gardner-Denver Co.*, 415 U.S. 36 (1974), that was severely narrowed by *Gilmer*. *See Duffield*, 144 F.3d at 1194-95. This argument relies on passages from the legislative history, which reflect the fact that at the time that § 118 was being drafted, *Gardner-Denver* was widely interpreted as prohibiting any form of compulsory arbitration of Title VII claims. *See id.*; *Prudential Ins. Co. v. Lai*, 42 F.3d 1299, 1303 (9th Cir. 1994) (collecting cases). *Gilmer* later limited *Gardner-Denver* to its facts, concerning collective bargaining, a subject not implicated by Desiderio's appeal. *See Gilmer*, 500 U.S. at 35.

Because we find the text clear on its face, we do not reach these arguments based on legislative history. Where the text of a statute is unambiguous, we need not look at the legislative history. *See Ex Parte Collett*, 337 U.S. 55, 61 (1949). As a consequence, we do not find *Duffield*'s analysis persuasive with respect to the applicability of *Gardner-Denver*.

C. *What Gilmer and the FAA Require*

Gilmer states the general principle that arbitration agreements are enforceable with regard to statutory claims, "unless Congress itself has evinced an intention to preclude a waiver of judicial remedies for the statutory rights at issue [as indicated] in the text of the [statute], its legislative history, or an inherent conflict between arbitration and the [statute's] underlying purposes." 500 U.S. at 26. *Gilmer* found nothing in the text, legislative history, statutory framework or purposes of the ADEA demonstrated a congressional aim to preclude arbitration, and hence concluded that mandatory arbitration clauses were enforceable under the FAA with respect to claims under the ADEA. 500 U.S. at 26-27; *see also Shearson/Am. Express, Inc. v. McMahon*, 482 U.S. 220, 226-27 (1987) (applying the same searching test to RICO and the Securities Exchange Act of 1934); *Bird v. Shearson Lehman/Am. Express, Inc.*, 926 F.2d 116, 118 (2d Cir. 1991) (same with respect to claims under ERISA).

Although many circuits have attempted to simplify the *Gilmer* inquiry by assuming that Title VII and ADEA share parallel objectives because they are similar civil rights statutes, *see Cole*, 105 F.3d at 1468; *Alford*, 939 F.2d at 230;

Metz, 39 F.3d at 1487; *Patterson*, 113 F.3d at 837; *Bender*, 971 F.2d at 700, reliance on such an assumption does not accord with the detailed analysis of statutory text, history, and purposes required by *Gilmer* on a statute-by-statute basis. Thus, we undertake this same statute-by-statute analysis with regard to Title VII. We begin by noting that the burden is on Desiderio to show that Congress intended to preclude a waiver of a judicial forum for her statutory claims, *see Gilmer*, 500 U.S. at 26, keeping in mind that "questions of arbitrability must be addressed with a healthy regard for the federal policy favoring arbitration," *Moses H. Cone Mem'l Hosp. v. Mercury Const. Corp.*, 460 U.S. 1, 24 (1983). We pass to an in-depth look at Title VII.

II Title VII's Text, Legislative History, & Purposes

A. *Text*

The first step in interpreting a statute is to determine whether the language at issue has a "plain and unambiguous meaning with regard to the particular dispute in the case." *Robinson v. Shell Oil Co.*, 519 U.S. 337, 340 (1997). "The plainness or ambiguity of statutory language is determined by reference to the language itself, the specific context in which that language is used, and the broader context of the statute as a whole." *Id.* at 341. If the text is unambiguous, the inquiry is at an end and we need proceed no further. *See id.* at 340.

The relevant text in Title VII states that "[w]here appropriate and to the extent authorized by law, the use of . . . arbitration[ ] is encouraged to resolve disputes arising

under the Acts or provisions of Federal law amended by this Title." Civil Rights Act of 1991, § 118. We conclude — as did the Third, Fourth, and Seventh Circuits — that the text of § 118 evinces a plain Congressional purpose of encouraging arbitration of Title VII claims and not one of precluding such arbitration. *See Koveleskie*, 167 F.3d at 365; *Seus*, 146 F.3d at 182; *Austin*, 78 F.3d at 881-83. It follows that barring the application of mandatory arbitration agreements to Title VII claims would conflict with the express statutory term "encouraged" in § 118.

The Ninth Circuit in *Duffield* suggested, to the contrary, that the text of § 118 is ambiguous when viewed in light of the general purpose of the Civil Rights Act of 1991, namely, to provide "additional remedies" against intentional discrimination, such as more expansive fee-shifting provisions and added rights to a jury trial and to compensatory and punitive damages. 144 F.3d at 1193 (citing § 2 of the Act). *Duffield* then concluded that the goal of expanding remedies was at odds with compulsory arbitration, which would effectively limit a plaintiff's options. 144 F.3d at 1192-93.

We are unable to adopt the view expressed in *Duffield*. Compulsory arbitration does not defeat the right to compensatory and punitive damages, or fee shifting because an arbitrator is also empowered to grant this kind of relief. Moreover, it is untenable to contend that compulsory arbitration conflicts with the Act's provision for the right to a jury trial, because *Gilmer* ruled that compulsory arbitration clauses could be enforced in claims under the ADEA, a statute that explicitly provides for jury trials. *See Rosenberg*,

170 F.3d at 11. Nor are we convinced that the underlying purposes of Title VII and the 1991 Civil Rights Act inherently conflict with the imposition of compulsory arbitration. We conclude therefore that the word "encouraged" is free of ambiguity when viewed in the context of the purpose of the statute.

B. *Legislative History Not Considered*

As Desiderio correctly notes, however, there is express language in the legislative history that suggests a congressional purpose to preclude mandatory arbitration of Title VII claims. For instance, two House Committee reports stated with respect to § 118 that "the Committee believes that any agreement to submit disputed issues to arbitration . . . in an employment contract, *does not preclude the affected person from seeking relief under the enforcement provisions of Title VII.*" H.R. Rep. No. 102-40(I), at 97 (1991) (House Committee on Education and Labor) (emphasis added), *reprinted in* 1991 U.S.C.C.A.N. 549, 635; H.R. Rep. No. 102-40(II) at 41 (House Judiciary Committee) (same), *reprinted in* 1991 U.S.C.C.A.N. 694, 735. One report further explained that § 118 "encourag[ed] the use of alternative means of dispute resolution to supplement, rather than supplant, the rights and remedies provided by Title VII," and that a Republican version of § 118 was rejected specifically because it "encourag[ed] the use of [arbitration] in place of judicial resolution . . . [and thus] employers could refuse to hire workers unless they signed a binding statement waiving all rights to file Title VII complaints." H.R. Rep. No. 102-40(I) at 104, *reprinted in* 1991 U.S.C.C.A.N. at 642.

Appendix A

While the language cited from the Committee reports suggests the preservation of the right to a judicial remedy under Title VII, such language is not found in the text of the statute. Rather, the Act says that the use of arbitration is to be "encouraged." We recognize that Congress' aim to foster arbitration, by itself, does not thereby require us to preserve an agreement waiving rights to a judicial forum. But, we assume, as does the Supreme Court, that the drafters of Title VII and the amendments introduced in the Act were well aware of what language was required for Congress to evince an intent to preclude a waiver of judicial remedies. In construing Title VII, the absence of that language is a meaningful omission. Moreover, the substantive rights found in the statute are not in any way diminished by our holding that arbitration may be compelled in this case, since only the forum — an arbitral rather than a judicial one — is affected, and plaintiff's rights may be as fully vindicated in the former as in the latter. As a result, and primarily because we find the language of the statute to be clear, we need not consider the inconsistent legislative history. *See Ex Parte Collett*, 337 U.S. at 61.

Because the text of Title VII does not square with its legislative history, appellant's argument comes down to nothing more than the poet's lament: The saddest words of tongue and pen are "it might have been, More sad are these we daily see; It is, but it hadn't ought to be." F. Brete Harte, *Mrs. Judge Jenkins*, *in Political Works*, 265, 267 (1872). In sum, we hold that Desiderio has not met her burden of showing that with respect to claims under Title VII, Congress intended to preclude the waiver of judicial remedies. Accordingly, the arbitration provision in Form U-4 may be applied to Desiderio's Title VII claims.

Appendix A

III Constitutional Claims

Plaintiff insists that the mandatory arbitration clause in Form U-4 unconstitutionally requires her to forfeit her Fifth Amendment right to due process, her Seventh Amendment right to a jury trial, and her right to an Article III judicial forum to assert her right to employment as a broker-dealer in the securities industry. We agree with the district court that these constitutional arguments all fail because the requisite state action is absent.

A. *NASD is a Private Entity*

A threshold requirement of plaintiff's constitutional claims is a demonstration that in denying plaintiff's constitutional rights, the defendant's conduct constituted state action. *See United States v. International Bhd. of Teamsters*, 941 F.2d 1292, 1295 (2d Cir. 1991). The NASD is a private actor, not a state actor. It is a private corporation that receives no federal or state funding. Its creation was not mandated by statute, nor does the government appoint its members or serve on any NASD board or committee. Moreover, the fact that a business entity is subject to "extensive and detailed" state regulation does not convert that organization's actions into those of the state. *Jackson v. Metropolitan Edison Co.*, 419 U.S. 345, 350 (1974) (extensively regulated public utilities are not state actors). Indeed, we have already ruled that the New York Stock Exchange — a self-regulatory private organization like the NASD — is not a state actor. *See United States v. Solomon*, 509 F.2d 863, 867-71 (2d Cir. 1975); *see also First Jersey Secs., Inc. v. Bergen*, 605 F.2d 690, 699 n.5 (3d Cir. 1979) (NASD is not a state agency).

B. *Nexus Required for State Action by Private Entities*

At the same time we recognize that private entities may be held to constitutional standards if their actions are "fairly attributable" to the state. *Lugar v. Edmondson Oil Co.*, 457 U.S. 922, 937 (1982). Several criteria for satisfying this standard have been established

> First, . . . [t]he complaining party must . . . show that there is a sufficiently *close nexus* between the State and the challenged action . . . . [C]onstitutional standards are invoked *only when it can be said that the State is responsible for the specific conduct* of which the plaintiff complains. . . .
>
> Second, . . . a State normally can be held responsible for a private decision *only when it has exercised coercive power or has provided such significant encouragement*, either overt or covert, that the choice must in law be deemed to be that of the State. *Mere approval . . . is not sufficient* to justify holding the State responsible for those initiatives . . . .

Blum v. Yaretsky, 457 U.S. 991, 1004-05 (1982) (emphases added).

Notably, *Blum* requires a nexus between the state and the *specific* conduct of which plaintiff complains. Here the nub of Desiderio's complaint is her challenge to the arbitration clause contained in the Form U-4. But no SEC

rule or action that has been called to our attention encourages the NASD to compel arbitration. *See Merrill Lynch, Pierce, Fenner & Smith v. Ware*, 414 U.S. 117, 135-36 (1973) ("[T]here is nothing in the [Securities Exchange Act of 1934] and there is no Commission rule or regulation that specifies arbitration as the favored means of resolving employer-employee disputes."); 17 C.F.R. § 240.15b7-1 (nothing in the 1993 SEC regulation text mentioning arbitration). Moreover, the arbitration clause in Form U-4 was drafted by the NASD in cooperation with other self-regulatory organizations, with no encouragement from the SEC. *See Adoption of Form U-4*, Exchange Act Rel. No. 11424, 7 S.E.C. Dkt. 2, 1975 WL 19312, at *2 (May 16, 1975).

Concededly, after Form U-4 was drafted, it was subject to approval by the SEC, from which fact plaintiff infers that state action is present. Simply because the SEC approved the arbitration clause in Form U-4 is not enough. As *Blum* emphasizes, a state is responsible for a private decision only where it exercised coercive power or provided significant encouragement. 457 U.S. at 1004-05. The SEC's "[m]ere approval" of Form U-4 is "not sufficient" to justify holding the state liable for the effects of the arbitration clause. *Id.* at 1004.

Consequently, we find no state action in the application or enforcement of the arbitration clause of Form U-4. This conclusion is consistent with our holding in *Albert v. Carovano*, 851 F.2d 561 (2d Cir. 1988) (*en banc*). In *Albert*, state law required a private college to formulate a disciplinary code and have it approved by the state. *Id.* at 564, 567. We held that the college's disciplining of a student was not state

action because the state law did not specifically dictate or draft the content of the disciplinary rules. *See id.* at 567, 571.

IV Contract of Adhesion

Again, appellant insists that Form U-4 is unenforceable, because it is an unconscionable contract of adhesion. A contract or clause is unconscionable when there is an "absence of meaningful choice on the part of one of the parties together with contract terms which are unreasonably favorable to the other party." 8 Samuel Williston, *A Treatise on the Law of Contracts*, § 18:9, at 54 (Richard A. Lord ed., 4th ed. 1998); *see Seus*, 146 F.3d at 184 (same); *David L. Threlkeld & Co. v. Metallgesellschaft Ltd.*, 923 F.2d 245, 249 (2d Cir. 1991) (purpose of unconscionability doctrine is to prevent unfair surprise and undue oppression); *see also Rust v. Drexel Firestone Inc.*, 352 F. Supp. 715, 717 (S.D.N.Y. 1972) (discussing element of duress).

Form U-4 binds *both* parties to mandatory arbitration and may not be said to favor the stronger party unreasonably. Hence, it is not a contract of adhesion. As the Supreme Court emphasized in *Gilmer*, "[m]ere inequality in bargaining power" between employers and employees is not alone sufficient to hold arbitration agreements unenforceable. 500 U.S. at 33; *cf. Seus*, 146 F.3d at 184 (Form U-4 arbitration clause not a contract of adhesion); *Drayer v. Krasner*, 572 F.2d 348, 353-56 (2d Cir. 1978) (upholding industry-wide NYSE mandatory arbitration clause as reasonable).

Appendix A

V Private Right of Action for Pendant State Claims

Finally, Desiderio brings state law tort claims against the NASD for its alleged "arbitrary and capricious administration in having an unpublished method" for avoiding mandatory arbitration. Specifically, plaintiff warrants that an unnamed employee of NASD chose to remain "perversely . . . silent" about the fact that the NASD rules do not actually prohibit an agreement between the employer and employee, which provides at the request of the employee that employment disputes will be litigated in court. Nonetheless, we have previously held there is no private right of action available under the Securities Exchange Act to redress denials of membership in an exchange, or to challenge an exchange's failure to follow its own rules. *See Feins v. American Stock Exch., Inc.*, 81 F.3d 1215, 1216 (2d Cir. 1996); *Brawer v. Options Clearing Corp.*, 807 F.2d 297, 298-99 (2d Cir. 1986).

Plaintiff acknowledges that generally no private right of action exists, but maintains that the rule has a bad faith exception. Whether plaintiff properly raised this bad faith argument to the district court is subject to some doubt, but in any event we exercise our discretion to entertain it. *See Greene v. United States*, 13 F.3d 577, 586 (2d Cir. 1994) (appellate court has some discretion to address arguments not raised in district court).

In *Brawer*, we held that "a private cause of action against an exchange or a clearinghouse for failure to comply with one of its rules which requires an exercise of discretion, *if one exists at all*, may be brought only if it is premised upon

allegations of fraud or bad faith." 807 F.2d at 299 (emphasis added). But it is problematic whether the bad faith exception suggested in *Brawer* binds us with regard to the specific circumstances presented in the present case. We later clarified in *Feins* that no private right of action existed for "erroneous membership decisions of securities exchanges, whether made intentionally, negligently or otherwise." 81 F.3d at 1222. Because *Feins* is analogous to the present case, in that it addressed a denial of membership, it controls. No bad faith exception is therefore available to Desiderio in the present circumstances. In sum, plaintiff has no private right of action and her state law claims were accordingly properly dismissed.

CONCLUSION

For the reasons stated, we affirm the judgment appealed from without costs to either party.

Appendix A

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT
UNITED STATES COURT HOUSE
40 FOLEY SQUARE
NEW YORK 10007

At a stated Term of the United States Court of Appeals for the Second Circuit, held at the United States Courthouse in the City of New York, Foley Square, on the 22nd day of September, one thousand nine hundred and ninety-nine.

BEFORE: Hon. Amalya L. Kearse
Hon. Richard J. Cardamone
Hon. Chester J. Straub

Circuit Judges

Docket No. 98-6100

SUSAN A. DESIDERIO,

Plaintiff-Appellant,

– v –

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.,

Defendant-Appellee.

Appeal from the United States District Court for the Southern District of New York.

Appendix A

This cause came on to be heard on the transcript of record from the Southern District of New York and was argued by counsel.

ON CONSIDERATION WHEREOF, it is now hereby **ORDERED, ADJUDGED, and DECREED** that the judgment of said district court be and it hereby is affirmed in accordance with the opinion of this court. No costs to either party.

FOR THE COURT
Karen Greve Milton, Acting Clerk
By:

s/ Beth J. Meador
Beth J. Meador
Administrative Attorney

APPENDIX B — OPINION AND ORDER OF THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK DATED APRIL 22, 1998

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

97 Civ. 0312 (PKL)

SUSAN A. DESIDERIO,

Plaintiff,

– against –

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC. and SECURITIES AND EXCHANGE COMMISSION,

Defendants.

OPINION AND ORDER

* * *

LEISURE, *District Judge*:

Plaintiff Susan Desiderio claims that a provision in Form U-4, Uniform Application for Securities Industry Registration or Transfer ("Form U-4"), that requires arbitration of disputes between securities brokers and their firms violates her constitutional and statutory rights under U.S. CONST. amend. III, V, and VII; U.S. CONST. art. III; Title 42, United States Code ("U.S.C."), §§ 2000a, *et seq.* ("Title VII"); and 2 U.S.C. §§ 601, *et seq.* Plaintiff seeks a

declaratory judgment against defendant National Association of Securities Dealers, Inc., ("NASD"); the NASD requires securities firms to file Form U-4 upon employing registered securities industry representatives or other securities professionals. Plaintiff also seeks a mandatory injunction invalidating the predispute arbitration provision in Form U-4 (Count I). Furthermore, plaintiff claims that the NASD is liable for tortious interference with contract (Count II) and negligent infliction of emotional distress (Count IV). Finally, plaintiff alleges that defendant Securities and Exchange Commission ("SEC") arbitrarily and capriciously and in violation of Chapter 15 of the Securities Exchange Act of 1934 (the "Exchange Act"), 15 U.S.C. §§ 78o, *et seq.*, has allowed the NASD to require registered representatives to submit employment disputes to arbitration as a condition of employment. Defendants now move for judgment on the pleadings on all claims, pursuant to Rules 12(b)(6) and 12(b)(1) of the Federal Rules of Civil Procedure. For the reasons stated herein, the Court grants defendants' motions.

BACKGROUND

The NASD is a private not-for-profit corporation organized under the laws of Delaware, and is a self-regulatory organization registered with the SEC as a national securities association. Under Section 25 of the Exchange Act, the NASD is required to regulate the over-the-counter securities market, securities firms, and their registered representatives who buy and sell over-the-counter securities. The SEC must approve all of the NASD's rules and regulations, including those relating to arbitration and the registration of securities representatives.

Appendix B

The NASD also is required to maintain employment records regarding its member securities firms and their registered representatives. Pursuant to its authority to establish standards for the uniform licensing and registration of securities professionals, the NASD has approved Form U-4 for use in registering securities industry representatives employed by securities firms. The NASD is required to retain Form U-4 for the states in which a representative is registered to do business; all states permit the filing of registration forms with the NASD Central Registration Depository.

By signing Form U-4, a registrant agrees to comply with all rules and regulations for the organizations with which he or she seeks to register, and agrees to arbitrate employment disputes.[1] The NASD operates an arbitration forum that resolves disputes between securities brokers and their firms. The NASD Code of Arbitration Procedure, which governs the proceedings in the NASD arbitration forum, requires a written arbitration award and regulates the composition of the arbitration panel, the disclosure of information by the arbitrators, and the removal of arbitrators through challenges.

On March 18, 1996, plaintiff was hired by SunTrust Bank ("SunTrust") in Florida as a registered securities representative. As a condition of employment, plaintiff was required by state and federal law to execute a Form U-4 registration form. Plaintiff executed the Form U-4, but struck

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1. On August 7, 1997, the NASD decided to eliminate this mandatory arbitration provision. Plaintiff refused to sign the Form U-4 in 1996, and brought this action in January of 1997. As the arbitration requirement was in effect at all times relevant to this action, the change in NASD policy has no bearing on the case.

out a provision in the Form requiring her to arbitrate any dispute with SunTrust. The NASD allegedly advised SunTrust's compliance department that an altered form would not be permitted, but plaintiff refused to submit an unaltered Form U-4. SunTrust subsequently revoked its offer of employment because plaintiff could not become registered, and the altered Form U-4 never was submitted to the NASD. On January 15, 1997, plaintiff filed a Complaint instituting the instant action and asserting that jurisdiction in this Court is proper pursuant to 28 U.S.C. §§ 1331, 1332, 1367, and the Administrative Procedure Act ("APA"), 5 U.S.C. § 701 *et seq*. Defendants now move for judgment on the pleadings.

DISCUSSION

I. *Standard for Judgment on the Pleadings*

When deciding a defendant's motion for judgment on the pleadings pursuant to either Fed. R. Civ. P. 12(b)(1) or 12(b)(6), a court may grant the motion "only where it appears beyond doubt that the plaintiff can prove no set of facts in support of his claim which would entitle him to relief." *Northrop v. Hoffman of Simsbury, Inc.*, 134 F.3d 41, 44 (2d Cir. 1997) (internal quotation omitted); *see also Jaghory v. New York State Department of Education*, 131 F.3d 326, 329 (2d Cir. 1997). In considering such a motion, the court "must accept as true the facts alleged in the complaint and draw all reasonable inferences in the plaintiff's favor." *Northrop*, 134 F.3d at 43; *see also Jaghory*, 131 F.3d at 329.

Appendix B

II. *Count I*

The Court first finds that the NASD is not a state actor and consequently could not violate plaintiff's Fifth Amendment due process rights. *See Public Utilities Commission v. Pollak*, 343 U.S. 451, 461 (1952) (finding that the Fifth Amendment "applies to and restricts only the Federal Government and not private persons"). The NASD is a private corporation, does not receive federal funding, and is not subject to any requirement that members of the NASD Board of Governors or members of the NASD Regulation, Inc. Board of Directors be government officials or appointed by a government official. Federal courts consistently have held that the NASD and other self-regulatory agencies are not state actors either in regulating industry pursuant to their statutory duties or in sponsoring arbitration fora that employ rules regulated by the SEC.[2]

The Court further concludes that Form U-4's provision subjecting federal statutory claims to mandatory arbitration is not unconstitutional. In *Gilmer v. Interstate/Johnson-Lane Corp.*, 500 U.S. 20 (1991), the United States Supreme Court upheld the legality of the mandatory predispute arbitration

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2. *See United States v. Solomon*, 509 F.2d 863, 869 (2d Cir. 1975) (finding no agency relationship between the New York Stock Exchange and the SEC); *see also First Jersey Securities, Inc. v. Bergen*, 605 F.2d 690, 699 n.5 (3d Cir. 1979) (the NASD is not a state agency); *Datek Securities Corp. v. National Association of Securities Dealers, Inc.*, 875 F. Supp. 230, 234 (S.D.N.Y. 1995); *Cremin v. Merrill, Lynch, Pierce, Fenner & Smith*, No. 96-3773, 1997 U.S. Dist. WL 88195, at *9 (N.D. Ill. Feb. 27, 1997).

provision in Form U-4 (used by the New York Stock Exchange ("NYSE")) in the face of arguments implicating the Seventh Amendment and Article III to the U.S. Constitution. The Court affirmed the broad sweep of the Federal Arbitration Act ("FAA") and noted that the exclusion from the FAA of contracts of employment does not apply to the arbitration provision in Form U-4, which is a contract with the securities exchanges. *See id.* 500 U.S. at 24-25 n.2.[3]

The plaintiff in *Gilmer* argued that the arbitration process and arbitration panel were biased and that the arbitration procedures were inadequate. The Court rejected this contention, holding that the NYSE arbitration rules sufficiently protected against biased panels and insured adequate resolution of the plaintiff's substantive rights outside of a judicial forum. *See id.* at 28-31.[4] The Court also rejected the argument that inequities in bargaining power between employers and employees justify holding arbitration agreements unenforceable, and held that the NYSE's requirement of a written arbitration award was sufficient. *See id.* at 28-30, 33. Because the arbitration rules analyzed and upheld by the Court in *Gilmer* are equivalent to provisions in the NASD Arbitration Code, the Court in effect

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3. The Court specifically found that mandatory arbitration of claims under the Age Discrimination and Employment Act of 1967 ("ADEA") was not precluded by the text, history, or purpose of the ADEA. *See id.* at 27.

4. *See also Kuehner v. Dickinson & Co.*, 84 F.3d 316, 320 (9th Cir. 1996) (absence of jury trial does not afford a basis for declining to enforce agreement to arbitrate, because right to jury trial is not substantive).

has rejected Desiderio's claims that the NASD arbitration requirement violates her constitutional rights.

Although neither the Supreme Court nor the Court of Appeals for the Second Circuit has held specifically that the mandatory arbitration clause of Form U-4 can apply to a claim under Title VII, the weight of authority from other circuits clearly supports such a conclusion.[5] Moreover, in *Genesco, Inc. v. T. Kakiuchi & Co., Ltd.*, 815 F.2d 840 (2d Cir. 1987), the Second Circuit held that a claim is subject to arbitration if (1) the parties agreed to arbitrate, (2) the agreement was intended by the parties to apply to that type of claim, (3) Congress intended the claim(s) to be arbitrable (when federal statutory claims are asserted), and (4) the court

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5. *See Bender v. A.G. Edwards & Sons, Inc.*, 971 F.2d 698, 700 (11th Cir. 1992) (finding that Title VII claims are subject to compulsory arbitration where plaintiff has signed Form U-4); *see also Mago v. Shearson Lehman Hutton, Inc.*, 956 F.2d 932, 935 (9th Cir. 1992) (finding that as Congress did not intend to preclude arbitration of Title VII claims, plaintiff's claims for sexual harassment and gender discrimination were subject to arbitration as provided in her employment application); *Patterson v. Tenet Healthcare, Inc.*, 113 F.3d 832, 837 (8th Cir. 1997) (Title VII claims are subject to individual consensual agreements to arbitrate); *Willis v. Dean Witter Reynolds, Inc.*, 948 F.2d 305, 307 (6th Cir. 1991) (finding that the FAA and arbitration provisions of the Securities Registration Form applied to plaintiff's Title VII claims); *Alford v. Dean Witter Reynolds, Inc.*, 939 F.2d 229, 230 (5th Cir. 1991) (holding that Title VII claims are subject to arbitration under the FAA); *Great Western Mortgage Corp. v. Peacock*, 110 F.3d 222, 229 (3d Cir. 1997) (finding that "more than a disparity in bargaining power is needed in order to show that an arbitration agreement was not entered into willingly").

need not stay the balance of the proceedings pending arbitration (when not all of the claims are arbitrable). *See* 815 F.2d at 844. Execution of the Form U-4 inherently represents an agreement to arbitrate employment claims, and other courts that have considered the issue have ruled that the predispute arbitration clause in the Form U-4 encompasses Title VII claims and compels their arbitration.[6] Thus, application of the standard set forth by the Second Circuit in *Genesco* leads the Court to the conclusion reached by so many courts that have considered the issue: it violates no constitutional provision to apply a mandatory arbitration clause to a claim under Title VII.

Plaintiff's reliance on the decisions in *Prudential Insurance Co. of America v. Lai*, 42 F.3d 1299 (9th Cir. 1994) and *Rosenberg v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, No. 96-12267, 1998 U.S. Dist. WL 81907 (D. Mass. Jan. 26, 1998) is misplaced. In *Lai*, the Court of Appeals for the Ninth Circuit found that the plaintiffs did not knowingly waive their right to litigate Title VII claims in court pursuant to signing Form U-4 because the plaintiffs were not told what they were signing, were not permitted to read the Form, were not aware that the Form contained an arbitration clause, and were not given a copy of the NASD Manual, which contained the applicable arbitration rules. *See Lai*, 42 F.3d at 1301, 1305. The instant case is readily distinguishable. As an initial

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6. *See Hall v. Metlife Resources*, No. 94-0358, 1995 U.S. Dist. WL 258061 (S.D.N.Y. May 3, 1995); *see also Scher v. Equitable Life Assurance Society of the United States*, 866 F. Supp. 776 (S.D.N.Y. 1994); *Scott v. Merrill, Lynch, Pierce, Fenner & Smith, Inc.*, No. 89-3749, 1992 U.S. Dist. WL 245506 (S.D.N.Y. Sept. 14, 1992).

matter, Desiderio is familiar with the arbitration clause in Form U-4 and with the NASD Arbitration Code. Thus, unlike the plaintiffs in *Lai*, Desiderio was aware that by signing the Form U-4, she would waive her right to litigate employment disputes in court. *Lai* also is distinguishable in that when the events relevant to the instant action occurred, the NASD arbitration rule in effect clearly covered employment disputes. In contrast, the NASD rule at issue in *Lai* was an earlier version that did not specifically require arbitration of employment disputes. *See id.* at 1305. Thus, the conclusions of the *Lai* court have little bearing on the issue in dispute here.

Nor does the Court place great stock in the decision in *Rosenberg*. The *Rosenberg* court denied a defendant's motion to compel arbitration of a plaintiff's Title VII claims on the ground that the NYSE arbitration forum was structurally biased in favor of securities firms. *See Rosenberg*, 1998 WL 81907 at *22. The court concluded that there existed structural bias in the practice of having arbitrators selected by the Director of Arbitration and the Chairman of the Board of the NYSE, which the court found to be dominated by securities industry representatives. *See id.* at *19. In contrast, the NASD Code and the structure of the NASD and of NASD Regulation, Inc., provide for selection of a majority of arbitrators from outside of the securities industry. As the weight of authority clearly favors upholding the arbitration provision in Form U-4 and because the cases cited by plaintiff are materially distinguishable from the instant case, the Court concludes that the NASD's arbitration requirement is constitutional and that Count I therefore does not state a claim upon which relief can be granted.

III. *Counts II and IV*

Plaintiff alleges that, under Florida law, the NASD tortiously interfered with her employment contract with SunTrust by requiring that plaintiff agree to the mandatory arbitration provision in Form U-4 and by causing SunTrust to terminate plaintiff's employment when she refused to agree to the provision. *See* Complaint at ¶ 41. Plaintiff also claims that the NASD negligently inflicted emotional distress upon plaintiff by causing SunTrust to terminate her employment. *See id.* at ¶ 59. However, the Exchange Act provides no express private right of action against the NASD for common law claims or for claims arising from the NASD's statutory function as a securities regulator.[7] Accordingly, the Court must dismiss Counts II and IV for failure to state a claim upon which relief can be granted.

IV. *Count III*

Plaintiff's claim against the SEC fails because the United States has not waived sovereign immunity and because plaintiff has neither exhausted her administrative remedies nor sought judicial review in the proper court. As a sovereign, the United States is not subject to suit without its consent.

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7. *See Mihalakis v. Pacific Brokerage Services Inc.*, No. 91-994, 1991 U.S. Dist. WL 280236, at *4 (S.D.N.Y. Dec. 23, 1991) (finding that the Exchange Act does not create a private right of action against the NASD); *see also Meyers v. National Association of Securities Dealers, Inc.*, No. 95-75077, 1996 U.S. Dist. LEXIS 6044, at *13-14 (E.D. Mich. March 29, 1996) (holding that no private right of action against the NASD exists under the Exchange Act for alleged tortious interference with contract).

See Lehman v. Nakshian, 453 U.S. 156, 160 (1981). Courts may only exercise jurisdiction over suits against the United States and its agencies if Congress has waived sovereign immunity by statute; the federal government and federal agencies may be sued only in the specific manner enumerated by Congress. *See Federal Deposit Insurance Corp. v. Meyer*, 510 U.S. 471, 475 (1994); *see also United States v. Dalm*, 494 U.S. 596, 608 (1990); *Soriano v. United States*, 352 U.S. 270, 276 (1957). As neither 28 U.S.C. § 1331 nor 28 U.S.C. § 1332 constitutes a waiver of sovereign immunity,[8] plaintiff only can obtain judicial review of SEC rules or of the SEC's approval of the rules of a self-regulatory organization such as the NASD under the APA. The APA specifies that "[t]he form of proceeding for judicial review is the special statutory review proceeding relevant to the subject matter in a court specified by statute." 5 U.S.C. § 703.

Section 25 of the Exchange Act, which governs the "form of proceeding for judicial review" adverted to in 5 U.S.C. § 703, requires that any party aggrieved or adversely affected by the entry of an order or promulgation of a rule must file a written petition with a United States Court of Appeals within 60 days after entry of the order or rule. *See* 15 U.S.C. §§ 78y(a)(1), (b)(1). The SEC approved the most recent NASD rule change regarding mandatory arbitration in 1993; plaintiff, however, did not file a petition within 60 days of

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8. *See Mack v. United States*, 814 F.2d 120, 122 (2d Cir. 1987) (finding that the general jurisdictional statute does not waive sovereign immunity); *see also Weeks Construction, Inc. v. Oglala Sioux Housing Authority*, 797 F.2d 668, 676 n.10 (8th Cir. 1986) (finding that the diversity jurisdiction statute does not allow action against United States).

the approval and has not filed the instant Complaint in the court prescribed by statute. Nor has plaintiff petitioned the SEC pursuant to 5 U.S.C. § 553(e) to establish a rule overturning or compelling modification of the NASD's arbitration rules.[9] As plaintiff has not complied with the Exchange Act and has not exhausted her administrative remedies by petitioning the SEC, the Court lacks subject matter jurisdiction over the claim asserted in Count III of the Complaint. Therefore, pursuant to Fed. R. Civ. P. 12(b)(1), the Court must dismiss Count III as well.

CONCLUSION

For the reasons stated, *supra*, defendants' motions to dismiss all counts of the Complaint for failure to state claims pursuant to Rules 12(b)(6) and 12(b)(1) of the Federal Rules of Civil Procedure are HEREBY GRANTED.

SO ORDERED.

New York, New York
April 22, 1998

s/ Peter K. Leisure
U.S.D.J.

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9. *Cf. Brown v. Secretary of Health and Human Services*, 46 F.3d 102, 113-114 (1st Cir. 1995) (party applying for Aid to Families with Dependent Children (AFDC) benefits should have exhausted administrative remedies by seeking amendment to regulation pursuant to 5 U.S.C. § 553(e), especially where party sought to raise factual and policy issues over which Congress has vested agency with primary discretion).

APPENDIX C — JUDGMENT OF THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK DATED AND FILED APRIL 23, 1998

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

97 CIVIL 0312(PKL)

SUSAN A. DESIDERIO,

Plaintiff,

– against –

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC., and SECURITIES AND EXCHANGE COMMISSION,

Defendants.

JUDGMENT

Defendants having moved to dismiss the Complaint pursuant to FRCP 12(b), and the said motion having come before the Honorable Peter K Leisure, United States District Judge, and the Court thereafter, on April 22, 1998 having issued its Opinion (80478) and Order granting defendants' motions to dismiss the Complaint for failure to state a claim, it is,

ORDERED, ADJUDGED AND DECREED: That for the reasons stated in the Court's Opinion (80478) and Order

dated April 22, 1998, defendants' motions to dismiss the Complaint for failure to state a claim be and are hereby granted.

DATED: New York, New York
April 23, 1998

JAMES M. PARKISON
Clerk of Court

By: s/ [illegible]
Deputy Clerk

APPENDIX D — ORDER OF THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT DENYING PETITION FOR REHEARING DATED AND FILED NOVEMBER 2, 1999

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT
UNITED STATES COURT HOUSE
40 FOLEY SQUARE
NEW YORK 10007

KAREN GREVE MILTON
ACTING CLERK

At a stated Term of the United States Court of Appeals for the Second Circuit, held at the United States Courthouse, Foley Square, in the City of New York, on the 2nd day of November one thousand nine hundred and ninety-nine

Present:

Hon. RICHARD J. CARDAMONE

Hon. AMALYA L. KEARSE

Hon. CHESTER J. STRAUB

Docket No. 98-6100

Desiderio,

Plaintiff-Appellant,

v

Appendix D

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC. and SECURITIES EXCHANGE COMMISSION,

Defendant-Appellee.

A petition for panel rehearing having been filed herein by The appellant, Susan A. Desiderio

Upon consideration thereof, it is
Ordered that said petition be and it hereby is **DENIED.**

FOR THE COURT
KAREN GREVE MILTON,
Acting Clerk

By: s/ Beth J. Meador
Beth J. Meador,

APPENDIX E — RELEVANT STATUTES AND REGULATION

FEDERAL ARBITRATION ACT (9 U.S.C. §§ 1, et seq.)

§ 1. "Maritime transactions" and "commerce" defined; exceptions to operation of title

* * *

. . . nothing herein contained shall apply to contracts of employment of seamen, railroad employees, or any other class of workers engaged in foreign or interstate commerce.

* * *

§ 2. Validity, irrevocability and enforcement of agreements to arbitrate

A written provision in any maritime transaction or a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction, or the refusal to perform the whole or any part thereof, or an agreement in writing to submit to arbitration an existing controversy arising out of such a contract, transaction, or refusal, shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.

* * *

Appendix E

§ 3. Stay of proceedings where issue therein referable to arbitration

If any suit or proceeding be brought in any of the courts of the United States upon any issue referable to arbitration under an agreement in writing for such arbitration, the court in which such suit is pending, upon being satisfied that the issue involved in such suit or proceeding is referable to arbitration under such an agreement, shall on application of one of the parties stay the trial of the action until such arbitration has been had in accordance with the terms of the agreement, providing the applicant for the stay is not in default in proceeding with such arbitration.

* * *

§ 9. Award of arbitrators; confirmation; jurisdiction; procedure

If the parties in their agreement have agreed that a judgment of the court shall be entered upon the award made pursuant to the arbitration, and shall specify the court, then at any time within one year after the award is made any party to the arbitration may apply to the court so specified for an order confirming the award, and thereupon the court must grant such an order unless the award is vacated, modified, or corrected as prescribed in sections 10 and 11 of this title. If no court is specified in the agreement of the parties, then such application may be made to the United States court in and for the district within which such award was made. Notice of the application shall be served upon the adverse party, and thereupon the court shall have jurisdiction of such

party as though he had appeared generally in the proceeding. If the adverse party is a resident of the district within which the award was made, such service shall be made upon the adverse party or his attorney as prescribed by law for service of notice of motion in an action in the same court. If the adverse party shall be a nonresident, then the notice of the application shall be served by the marshal of any district within which the adverse party may be found in like manner as other process of the court.

* * *

§ 10. Same; vacation; grounds; rehearing

(a) In any of the following cases the United States court in and for the district wherein the award was made may make an order vacating the award upon the application of any party to the arbitration —

(1) Where the award was procured by corruption, fraud or undue means.

(2) Where there was evident partiality or corruption in the arbitrators, or either of them.

(3) Where the arbitrators were guilty of misconduct in refusing to postpone the hearing, upon sufficient cause shown, or in refusing to hear evidence pertinent and material to the controversy, or of any other misbehavior by which the rights of any party have been prejudiced.

(4) Where the arbitrators exceeded their powers, or so imperfectly executed them that a mutual, final, and definite award upon the subject matter submitted was not made.

(5) Where an award is vacated and the time within which the agreement required the award to be made has not expired the court may, in its discretion, direction a rehearing by the arbitrators. . . .

* * *

CIVIL RIGHTS ACT OF 1991, Pub. L. 102-166 (42 U.S.C. § 1981a)

Sec. 1981a. Damages in cases of intentional discrimination in employment

(a) Right of recovery

(1) Civil rights

In an action brought by a complaining party under section 706 or 717 of the Civil Rights Act of 1964 (42 U.S.C. 2000e-5, 2000e-16) against a respondent who engaged in unlawful intentional discrimination (not an employment practice that is unlawful because of its disparate impact) prohibited under section 703, 704, or 717 of the Act (42 U.S.C. 2000e-2, 2000e-3, 2000e-16), and provided that the complaining party cannot

recover under section 1981 of this title, the complaining party may recover compensatory and punitive damages as allowed in subsection (b) of this section, in addition to any relief authorized by section 706(g) of the Civil Rights Act of 1964, from the respondent. . . .

(b) Compensatory and punitive damages

(1) Determination of punitive damages

A complaining party may recover punitive damages under this section against a respondent (other than a government, government agency or political subdivision) if the complaining party demonstrates that the respondent engaged in a discriminatory practice or discriminatory practices with malice or with reckless indifference to the federally protected rights of an aggrieved individual. . . .

(c) Jury trial

If a complaining party seeks compensatory or punitive damages under this section —

(1) any party may demand a trial by jury; and

(2) the court shall not inform the jury of the limitations described in subsection (b)(3) of this section. . . .

* * *

Appendix E

SEC Regulation, 17 C.F.R. § 240.15b7-1 promulgated May 11, 1993

Sec. 240.15b7-1 Compliance with qualification requirements of self-regulatory organizations.

No registered broker or dealer shall effect any transaction in, or induce the purchase or sale of, any security unless any natural person associated with such broker or dealer who effects or is involved in effecting such transaction is registered or approved in accordance with the standards of training, experience, competence, and other qualification standards (including but not limited to submitting and maintaining all required forms, paying all required fees, and passing any required examinations) established by the rules of any national securities exchange or national securities association of which such broker or dealer is a member or under the rules of the Municipal Securities Rulemaking Board (if it is subject to the rules of that organization).

[58 FR 27658, May 11, 1993]

* * * *